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IN THE
SUPREME COURT OF THE UNITED STATES
October Term, 1972

No. 72-496

MORRIE BENSON, Petitioner,

v.

ARTHUR NEWMAN, et al., Respondents.

BRIEF FOR PLAINTIFFS-RESPONDENTS IN OPPOSITION TO PETITION FOR CERTIORARI

The decision below of the United States Court of Appeals for the Second Circuit (A. 20), not yet officially reported, appears at CCH Fed. Sec. L. Rep. ¶ 93,547.

QUESTION PRESENTED

In light of the undisputed substantial legal doubts surrounding the validity of plaintiffs' claim and the proper measure of damages, did the District Court abuse its discretion under FRCP 23.1 in approving the $5 million settlement of these stockholders' derivative actions?

STATEMENT OF THE CASE

These actions are three consolidated stockholders' derivative suits brought on behalf of defendant-respondent The Dreyfus Fund Incorporated ("the Fund"), a diversified open-end investment company or mutual fund registered under the Investment Company Act of 1940 ("the Act"). The real defendants, respondents here, are The Dreyfus Corporation ("the Corporation"), which was the Fund's investment adviser and principal underwriter; the Corporation's former parent, Dreyfus & Co. ("the Partnership"); and a number of individuals who were partners in the Partnership or held various positions with the Fund, the Corporation or both. The District Court's jurisdiction was based on the Act and the principles of pendent jurisdiction.

In October 1965 the Partnership distributed the stock of the Corporation to its partners. The latter thereupon sold 88% of the stock to underwriters for some $41 million, and the underwriters resold the stock to the public. By reason of §§ 15(a)(4) and 2(a)(4) of the Act (A. 8), these stock transfers terminated the Corporation's investment advisory contract with the Fund, but the stockholders of the Fund, acting upon defendants' recommendation, reinstated the contract. It was plaintiffs' principal claim that these transactions constituted a sale of the

Corporation's advisory office and that, under the rule of Rosenfeld v. Black, 445 F. 2d 1337 (2d Cir. 1971),* defendants are liable to the Fund for their "profit", i.e., the difference of about $35 million between the proceeds from the stock sale and the book value of the stock.**

After a full trial before Judge McLean, the parties agreed to settle the actions for $5 million. Following notice to the stockholders of the Fund and a full hearing, Judge McLean approved the settlement pursuant to FRCP 23.1, overruling the objections of petitioner and another stockholder (A. 10). Upon the objectors' appeal, the Second Circuit affirmed, finding that the District Court had not abused its discretion since the validity of plaintiffs' claim as well as the proper measure of recovery were open

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*A petition for certiorari in the Rosenfeld case was dismissed pursuant to Rule 60 of this Court, Lazard Freres & Co. v. Rosenfeld, Docket No. 71-771, Sept. 1, 1972. The Rosenfeld case has been settled with judicial approval, Rosenfeld v. Black, 336 F. Supp. 84 (SDNY 1972).

**Plaintiffs also alleged a claim for proxy misrepresentation, but the Courts below considered that claim as insubstantial (A. 15, 28-30), and petitioner does not rely on it.

to substantial legal doubts (A. 20). This is the decision of which petitioner seeks review by this Court.

REASONS FOR DENYING THE WRIT

The decision of the Court of Appeals discusses at length the substantial legal doubts surrounding the validity of plaintiffs' claim (A. 30-35) and the applicable measure of recovery (A. 35-38). Petitioner does not dispute the serious nature of these doubts,* but contends that this Court should resolve them.

The contention rests on a complete misconception of the issues under FRCP 23.1 In passing on the fairness of a proposed settlement, the "basic" task of the Court is "to compare the terms of the compromise with the likely rewards of litigation", Protective Committee v. Anderson, 390 U.S. 414, 424-25 (1968). In other words, "the strength of the case for plaintiffs on the merits [must be] balanced against the amount offered in

*These doubts are reinforced by a recent decision, Kukman v. Baum, CCH Fed. Sec. L. Rep. ¶ 93,602 (N.D. Ill., 7/10/72), which has refused to follow the Second Circuit's ruling in Rosenfeld v. Black, supra (445 F. 2d 1337).

settlement"; State of West Virginia v. Chas. Pfizer & Co., 440 F. 2d 1079, 1085-86 (2d Cir. 1971); Florida Trailer & Equip. Corp. v. Deal, 284 F. 2d 567, 571, 573 (5th Cir. 1960).

In the present case, the facts were virtually undisputed, but the applicable law was in doubt. The issue before the Courts below was, therefore, whether, in light of the substantial legal questions, the prospect of a $35 million recovery was sufficiently uncertain to justify a $5 million settlement. The resolution of that issue was committed to the informed discretion of the District Court (A. 26).* The District Court answered in the affirmative. The Court of Appeals agreed. Both courts engaged in a careful analysis of the legal problems and reached "an intelligent and objective opinion of the probabilities of ultimate success" (Protective Committee v. Anderson, supra, 390 U.S. at 424). Petitioner himself, as noted, does not dispute the grave character of the legal issues.

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*State of West Virginia v. Chas. Pfizer & Co., supra, 440 F. 2d 1079, 1085; Ace Heating & P. Co. v. Crane Co., 453 F. 2d 30, 34 (3rd Cir. 1971); Young v. Katz, 447 F. 2d 431, 432 (5th Cir. 1971).

Since the presence of unresolved legal questions was the very basis of the settlement, it would be the height of incongruity to undertake their resolution in these proceedings. In passing on a proposed settlement, the "court need not and should not reach any dispositive conclusions on the admittedly unsettled legal issues which the case raises", for the "very purpose of a compromise is to avoid the determination of sharply contested and dubious issues"; State of West Virginia v. Chas. Pfizer & Co., supra, 440 F. 2d at 1086. As the Fifth Circuit held in affirming the approval of a settlement, Florida Trailer & Equip. Co. v. Deal, supra, 284 F. 2d 567, 571-72:

> "Of course, the approval of a proposed settlement does not depend on establishing as a matter of legal certainty that the subject claim or counterclaim is or is not worthless or valuable. The probable outcome in the event of litigation, the relative advantages and disadvantages are, of course, relevant factors for evaluation. But the very uncertainties of outcome in litigation, as well as the avoidance of wasteful litigation and expense, lay behind the Congressional infusion of a power to compromise. This is a recognition of the policy of the law generally to encourage settlements. This could hardly be achieved if the test on hearing for

> approval meant establishing success or failure to a certainty. Parties should be hesitant to explore the likelihood of settlement apprehensive as they would then be that the application for approval would necessarily result in a judicial determination that there was no escape from liability or no hope of recovery and hence no basis for a compromise.
>
> "* * * *
>
> "Here there were many uncertainties, not the least of which was the novelty of [the] legal question."

In the posture of the present case, the grant of certiorari could serve no useful purpose. Petitioner, to be sure, asks this Court to decide authoritatively whether the sale of an investment advisory office is unlawful and, if so, what the proper measure of recovery is. The answer to these questions might be relevant if a final determination of the merits of the litigation were sought. It is irrelevant, however, to the only issue remaining in the case, the fairness of the settlement. The settlement is fair precisely because the legal issues in the case are unresolved and uncertain. To resolve them now could not affect the fairness of the settlement when made and approved; and while petitioner urges

this Court to furnish guidance for future similar cases, it is not the Court's province to issue advisory opinions.

CONCLUSION

The petition for a writ of certiorari should be denied.

October 8, 1972

Respectfully submitted,

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of counsel.